



CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

November 8, 2002

S. 2949

Aviation Security Improvement Act

*As reported by the Senate Committee on Commerce, Science, and Transportation
on September 30, 2002*

SUMMARY

S. 2949 would require the Federal Aviation Administration (FAA) to offer to insure air carriers for damage to aircraft hulls and injuries to passengers and crew that are the result of terrorist attacks. The bill would authorize the FAA to charge premiums for such insurance, but the rates charged would probably not adequately compensate the federal government for its added risk. Based on the difference between what the FAA would likely charge and the amount that CBO estimates would be necessary to compensate for the added risk the government would incur under the bill, we estimate that enacting S. 2949 would increase direct spending by \$300 million in 2003.

The bill also would impose new duties on the FAA, the Department of Justice (DOJ), and the Transportation Security Administration (TSA). S. 2949 would require the TSA to establish an industry-wide database of cargo shippers, a system for the regular inspection of air shipping facilities, and a security training program for air cargo handlers. In addition, the bill would authorize the TSA to use identification verification technologies to prevent intentional circumvention of airport security systems or procedures. S. 2949 would require the TSA and the FAA to evaluate the use of blast-resistant cargo containers. The bill also would subject all aliens seeking flight school training on small aircraft to background checks under procedures issued by DOJ. Finally, the bill would make several amendments to current TSA programs and would make noncitizens eligible to become federal screeners of air passengers and baggage. CBO has insufficient information from the Department of Transportation to estimate the cost of those provisions at this time, but the increase in TSA's costs subject to appropriation could be significant.

S. 2949 contains no intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would impose no costs on state, local, or tribal governments.

S. 2949 would impose private-sector mandates as defined in UMRA on carriers that transport cargo and facilities that provide flight training to foreign candidates. The cost to comply with those mandates would depend on the standards to be developed after enactment. However, based on information on current industry practices from the TSA and industry representatives, CBO expects that the costs to comply with the mandates would not exceed the annual threshold established by UMRA for private-sector mandates (\$115 million in 2002, adjusted annually for inflation).

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of S. 2949 is shown in the following table. The costs of this legislation fall within budget function 400 (transportation).

| | By Fiscal Year, in Millions of Dollars | | | | |
|---|--|------|------|------|------|
| | 2003 | 2004 | 2005 | 2006 | 2007 |
| CHANGES IN DIRECT SPENDING^a | | | | | |
| Estimated Budget Authority | 300 | 0 | 0 | 0 | 0 |
| Estimated Outlays | 300 | 0 | 0 | 0 | 0 |

a. The bill would also increase spending subject to appropriation, but CBO has not completed an estimate of those costs.

BASIS OF ESTIMATE

S. 2949 would make several changes related to FAA's insurance program for air carriers. Under current law, the FAA provides third-party war-risk (including terrorism) liability insurance to U.S. air carriers that covers losses above \$50 million. (Airlines purchase coverage for the first \$50 million in such damages from private insurers.) CBO estimates that the premiums currently charged by the FAA for this insurance coverage are insufficient to compensate the government for the risk of this program. Current law allows the FAA to charge less than the full amount necessary to compensate the government for risk. The FAA has chosen to exercise that discretion, in part because of the financial weakness of the airlines.

S. 2949 would require the FAA to continue to offer to insure air carriers against liabilities to third parties for damages due to acts of war or terrorism for 270 days after enactment. The

bill would require the FAA to offer such coverage on terms that are no less favorable than those currently in effect. In addition, the bill would require the FAA to provide new insurance against losses from damage to aircraft hulls and injuries to passengers and crew that result from acts of war or terrorism. It would direct the FAA to charge rates for that insurance that are comparable to those it currently charges.

By expanding federally provided insurance coverage for domestic air carriers, S. 2949 would expose the federal government to potentially huge liabilities. CBO has no basis for estimating the likelihood, amount, or timing of air carrier losses due to terrorist attacks. Instead, our estimate of the cost of this provision is based on the difference between what the FAA would charge to provide such insurance and the amount that we estimate would be necessary to compensate private-sector insurers for the risk the federal government would incur.

Extension of Current Third-Party War-Risk Insurance

S. 2949 would require the FAA to continue to provide air carriers with third-party war-risk insurance on terms that are no less favorable than the terms of policies in effect on June 19, 2002. CBO estimates that those premiums do not adequately compensate the government for the aggregate risk it has assumed through these insurance policies. Based on private rates for similar coverage, CBO estimates that the FAA would have to charge premiums of nearly \$500 million to adequately compensate the government for the risk of providing third-party war-risk insurance for domestic flights for 270 days in 2003. Subtracting the premiums that we estimate air carriers will pay the FAA, CBO estimates the net cost to the federal government of providing insurance at less than market rates will be about \$400 million in 2003. The FAA, however, already has the authority to continue to offer this insurance and has previously extended the availability of the coverage on six occasions. CBO expects that the agency will continue to do so for many months under current law. Therefore, even though we estimate that continuation of this insurance program has a significant cost, we expect that this cost will be incurred under current law.

Expansion of Aviation Insurance for Aircraft Hulls, Passengers, and Crew

S. 2949 would require the FAA to offer insurance coverage for losses or injuries to aircraft hulls, passengers, and crew members due to acts of war or terrorism for 270 days after enactment. Because the FAA currently has authority to offer such insurance but has chosen not to do so, we expect that the FAA would not offer it beyond the required 270 days.

Aircraft Hull Insurance. Based on information from air carriers and aviation insurers, CBO estimates that the insured value of the U.S. commercial fleet is about \$160 billion. Commercial insurance companies currently charge airlines less than 10 cents per \$100 of aircraft hull value for a full year of war-risk coverage. We assume that nearly 25 percent of such private-sector premiums are for commissions or other administrative costs that are not applicable to the federal government, and that insurers reduce premiums by about 25 percent in the years following a catastrophic loss as liquidity concerns ease. Hence, CBO estimates that the FAA would have to charge premiums of at least \$50 million to adequately compensate the government for the risk of insuring hulls for three-quarters of 2003.

Aviation Insurance for Passengers and Crew. Soon after September 11, 2001, the insurers of air carriers imposed a \$1.25 per passenger surcharge for providing war risk insurance coverage of passengers and crew. Based on the projected number of passengers in 2003, CBO estimates that domestic air carriers will pay private insurers roughly \$650 million for 270 days of coverage in 2003. (That premium also includes coverage of third-party liability for the first \$50 million in losses.)

We assume that nearly 25 percent of such private-sector premiums are for commissions or other administrative costs that are not applicable to the federal government, and that insurers reduce premiums by about 25 percent in the years following a catastrophic loss as liquidity concerns ease. Hence, CBO estimates that the FAA would have to charge premiums of about \$300 million to adequately compensate the government for the risk of providing the required insurance coverage.

Additional premiums for hull, passenger, and crew insurance. The bill would direct the FAA to charge an additional premium for new insurance that is comparable to the premium it charges for third-party coverage under current policies. On that basis, we estimate the agency would collect about \$50 million in premiums for insurance coverage of aircraft hulls, passengers, and crew members. Therefore, we estimate that the net cost to the federal government of providing insurance would be about \$300 million in 2003.

Spending Subject to Appropriation

CBO has insufficient information from the TSA at this time to estimate the bill's costs that are subject to appropriation, but they could be significant. The cost of most of these provisions would depend on how the bill is implemented by the TSA and what steps the agency would otherwise take (under current law) to ensure the safety of air cargo under its existing broad authority.

S. 2949 would require the TSA to establish an industry-wide database of air cargo shippers that use passenger aircraft. More than 50 air carriers transport air cargo on passenger aircraft. The largest carriers of air cargo may conduct business with nearly 2 million shippers per night. Based on the number of shippers that would need to be tracked and the amount that air carriers spend on their own systems to track shippers, CBO estimates that establishing and maintaining an industry-wide database of known shippers would cost several million dollars each year.

S. 2949 would require the TSA to establish systems to screen, inspect, or otherwise ensure the security of all air cargo transported in passenger aircraft. Under current law, the TSA is required to provide screening for cargo transported on passenger aircraft. Hence, this provision could reduce the costs of the TSA to the extent that it chooses to verify the security of air cargo in a manner that is less expensive than screening. The agency, however, is uncertain how this provision would be implemented and whether there would be any savings. Security experts that CBO consulted believe the most effective way to ensure the security of air cargo is to inspect the cargo just before it is loaded on a plane.

S. 2949 imposes many additional requirements on the TSA with respect to air cargo security, including security training of air cargo handlers, evaluating blast-resistant cargo containers, and stationing law enforcement officers in smaller airports. Under current law, the TSA has broad requirements to provide for air transportation security. To the extent that the provisions of S. 2949 would cause the TSA to change its plans, implementing the bill could result in significant additional costs. CBO has insufficient information from the Department of Transportation to identify how those provisions of S. 2949 would change the TSA's plans or how much those changes would cost.

ESTIMATED IMPACT ON THE PRIVATE SECTOR

S. 2949 would impose private-sector mandates as defined in UMRA on air carriers that transport cargo and on facilities that provide flight training to foreign candidates. The costs to comply with those mandates would depend on standards to be developed after enactment. However, based on information on current industry practices from the TSA and industry representatives, CBO expects that the costs to comply with the mandates would not exceed the annual threshold established by UMRA for private-sector mandates (\$115 million in 2002, adjusted annually for inflation).

S. 2949 would require air carriers that operate passenger aircraft and all-cargo aircraft to comply with new security procedures for cargo. In addition, the bill would require air carriers that operate all-cargo aircraft to have a security plan. Both the new security procedures and the requirements in the security plan would be based on standards to be set by the Under Secretary of Transportation for Security. Based on information on industry

practices from the TSA and representatives for air carriers transporting cargo, CBO expects that the costs of compliance would not be great.

Current law requires facilities that provide flight training to submit certain information to the Attorney General on foreign candidates requesting initial training to operate aircraft weighing 12,500 pounds or more. S. 2949 would require such training facilities to submit that information on foreign candidates requesting initial training on any aircraft, regardless of size. Based on information from the Department of Justice and representatives of flight training facilities, CBO estimates that the incremental cost to comply with this mandate would be minimal.

ESTIMATED IMPACT ON STATE, LOCAL, AND TRIBAL GOVERNMENTS

S. 2949 contains no intergovernmental mandates as defined in UMRA and would impose no costs on state, local, or tribal governments. Airports could be affected by several provisions that would require air carriers that transport cargo to install machinery and systems to enhance security. As a result, airports might need to find or create space to accommodate security improvements. Because of uncertainties about what requirements would be imposed on air carriers and how they would be implemented, CBO cannot predict how airports would be affected. We expect, however, that any resulting costs would not be large.

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